BEFORE

THE PUBLIC SERVICE COMMISSION OF

SOUTH CAROLINA

DOCKET NO. 95-1171-S - ORDER NO. 96-134

FEBRUARY 29, 1996

IN RE: Application of Brookside Sewer District for Approval of an Increase in Rates and Charges for Sewer Service.	))))	ORDER APPROVING RATES AND CHARGES

This matter comes before the Public Service Commission of South Carolina ("the Commission") by way of the Application of Brookside Sewer District ("Brookside" or "the Company") for approval of a new schedule of rates and charges. The Company's Application was filed pursuant to S.C. Code Ann. §58-5-240 (Supp. 1995) and 26 S.C. Code Ann.Regs.103-821 (1976) of the Commission's Rules of Practice and Procedure.

By letter dated October 10, 1995, the Commission's Executive Director instructed the Company to publish a prepared Notice of Filing, one time, in newspapers of general circulation in the area affected by the Company's Application. The Notice of Filing indicated the nature of the Company's Application and advised all interested parties desiring participation in the scheduled proceedings of the manner and time in which to file the appropriate pleadings to be included in the proceedings. The Company was also instructed to notify directly all customers affected by the proposed rates and charges. The Company filed with the Commission affidavits which indicated that the Company complied with the instructions of the Executive Director regarding the publication and mailing of the Notice of Filing. No Petitions to Intervene were received by the Commission, but a neighborhood petition with approximately 316 names opposing the amount of the proposed increase was received by the Commission.

The Commission Staff made on-site investigations of the Company's facilities, audited the Company's books and records, and gathered other detailed information concerning the Company's operations.

On January 11, 1996, a public hearing regarding the Company's Application was held in the Commission's hearing room at 111 Doctors Circle, Columbia, South Carolina. Pursuant to S.C. Code Ann. §58-3-95 (Supp.1995), a panel of three (3) Commissioners was designated to hear and rule on this matter. The panel consisted of Commissioners Bradley, Saunders, and Scott. Commissioner Bradley presided over the proceeding. John F. Beach, Esquire represented Brookside, and Florence P. Belser, Staff Counsel, represented the Commission Staff.

Brookside presented the testimony of Frank M. Nutt, owner of Brookside. The Commission Staff presented the testimony of William O. Richardson, Public Utilities Engineer III, and Joe Maready, Public Utilities Accountant. In addition, two (2) customers of Brookside, Cheryl Hampton and Guy Santa-Lucia, appeared and offered testimony as public witnesses.

After thorough consideration of the entire record in this case, including the testimony and all exhibits, and the applicable law, the Commission makes the following findings of fact and conclusions of law:

FINDINGS OF FACT

1. Brookside is a sewer utility providing sewer service to 420 customers in Brookside Village located in Spartanburg County, South Carolina, and Brookside is subject to the jurisdiction of the Commission pursuant to S.C. Code Ann. §58-5-10 (Supp.1995) et seq. Brookside's present rates and charges were approved in Docket No. 87-81-S, Order No. 88-738 dated July 26, 1988.

2. The Commission finds that the appropriate test year for use in this proceeding is the twelve month period ending December 31, 1994.

3. The Commission finds that the appropriate level of revenues for Brookside for the test year under present rates and after accounting and pro forma adjustments is $68,040.

4. The Commission finds that the Company's appropriate operating expenses for the test year, after accounting and pro forma adjustments are $86,985.

5. The Company's net operating income for the test year, after accounting and pro forma adjustments approved herein, is calculated to be ($18,945), and the Company's net income for return for the test year after accounting and pro forma adjustments approved herein is calculated to be ($18,945).

6. The Commission finds it appropriate to use the operating margin as its guide in determining the lawfulness of the Company's

proposed rates and for the fixing of just and reasonable rates.

7. Under the presently approved rates, Staff computed Brookside's operating margin, after interest and after the herein approved accounting and pro forma adjustments, to be (27.84%).

8. Brookside's proposed increase in rates and charges, after the herein approved accounting and pro forma adjustments, would result in an operating margin of 21.16%. The Commission finds an operating margin of 21.16% to be excessive and unreasonable. The Commission further finds an operating margin of 12.29% to be appropriate and reasonable and hereby approves an operating margin of 12.29%.

9. The Commission finds the appropriate level of operating revenues under the rates approved herein is $103,320, which reflects a net authorized increase in operating revenues of $35,280.

10. The Commission finds the appropriate operating expenses under the rates approved herein are $90,621.

11. The Commission finds the appropriate level of net operating income for return after accounting and pro forma adjustments under the rates approved herein is $12,699.

CONCLUSIONS OF LAW

1. Brookside is a company providing sewer service for compensation to 420 customers in Spartanburg County, South Carolina pursuant to Commission approved rates and charges. (See, Hearing Exhibit No. 4, p. 7 and Hearing Exhibit 5, p. 1.) As such, Brookside's operations in South Carolina are subject to the

jurisdiction of the Commission pursuant to S.C. Code §58-5-10 (Supp.1995). Brookside's current rates and charges were approved in Docket No. 87-81-S, Order No. 88-738 dated July 26, 1988. (See, Hearing Exhibit No. 5, p. 1.) This conclusion is jurisdictional in nature and is not being contested in this proceeding.

2. A fundamental principle of the ratemaking process is the establishment of a historical test year with the basis for calculating a utility's revenues and expenses and, consequently, the validity of the utility's requested rate increase. Integral to the use of a test year, representing normal operating conditions to be anticipated in the future, is the necessity to make normalizing adjustments to the historic test year figures. While the Commission considers a utility's proposed rate increase based upon occurrences within the test year, the Commission will also consider adjustments for any known and measurable out-of-test year changes in expenses, revenues, and investments, and will also consider adjustments for any unusual situations which occurred in the test year. See, Parker v. South Carolina Public Service Commission, 280 S.C. 310, 313 S.E.2d 290 (1984), citing City of Pittsburgh v. Pennsylvania Public Utility Commission, 187 P.A. Super. 341, 144 A.2d 648 (1958); Southern Bell v. The Public Service Commission, 270 S.C. 590, 244 S.E.2d 278 (1978).

The Company chose as its test year on which to present evidence of revenues and expenses the twelve month period ending December 31, 1994. (See, Amended Application, p. 3.) The

Commission Staff used the same period in calculating its adjustments. (See, Hearing Exhibit 5.) Based on the information available to the Commission, the Commission concludes, and therefore finds, that the test year ending December 31, 1994 is appropriate for the purposes of this rate request.

3. At present, Brookside charges a flat monthly rate of $13.50 for sewer service. Additionally, Brookside currently has approved a New Customer Set-Up Charge of $10.00 and a Notification of Disconnection Charge of $6.00. (See, Hearing Exhibit No. 4, p. 1.)

Based on the test year data, Brookside computed its test year revenues to be $65,472. Staff computed Brookside's test year revenues to be $68,040. Staff proposed to adjust test year revenues for end-of-period customers. Staff's adjustment of $2,902 annualizes the test year revenues for the number of customers at the end of the test year. Staff also proposed to adjust test year revenues by ($334) to remove "Interest Income" which is not subject to regulation by the Commission. At the hearing, counsel for Brookside stated that Brookside agreed with Staff's accounting adjustments with the exception of certain expense adjustments. The Commission concludes that Staff's adjustments are reasonable and therefore adopts Staff's adjustments to revenues as appropriate. The Commission also notes that Brookside did not take exception with Staff's adjustments to revenues.

4. As stated above, Brookside stipulated at the hearing that

it agreed with most of Staff's accounting adjustments. However, Brookside specifically stated that it did not agree with Staff's adjustments regarding (a) utilities and insurance associated with the Company's office; (b) rent allocated to the utility for the Company's office; (c) salary expense; and (d) rate case expense. The Commission will adopt all of Staff's accounting adjustments with which Brookside agreed and will address separately each of the adjustments with which Brookside disagreed.

(a) Regarding the utilities and insurance expense associated with the Company's office, the Company, by its Application, proposed to increase its annual expense by $4,450. Staff proposed an adjustment of $1,483, or 1/3 of the Company's adjustment. Staff witness Maready testified that in his opinion Brookside utilized 1/3 of the productive space in the building in which the office is housed, and that he therefore allowed 1/3 of the Company's proposed adjustment. At the hearing, Brookside introduced Hearing Exhibit No. 3 in support of a higher utilities and rent expense adjustment. Hearing Exhibit No. 3 presents an argument for an adjustment of $2,342. Hearing Exhibit No. 3 is less than the adjustment proposed in the Application, and the information contained in Hearing Exhibit No. 3 was not made available for Staff to verify during its audit of the Company and the test year. The Commission finds Staff's adjustment to be reasonable and hereby adopts Staff's adjustment.

(b) By its Application, Brookside included a rent expense of $3,900 for rent of the Company's office. Staff proposed an adjustment of $1,300 which is 1/3 of the Company's proposed adjustment. Staff witness Maready testified that the utility office is housed in a building within the Brookside Village subdivision which also houses other offices of the Nutt Corporation. Maready testified that he allowed 1/3 of the Company's proposed rent expense adjustment because he felt that the utility utilized approximately 1/3 of the productive space of the whole building. Brookside offered Hearing Exhibit No. 3 and the testimony of Mr. Nutt in support of its adjustment. Brookside offered that a rent expense of $3,900 per year, or $325 per month, was reasonable as the utility's portion of rent on the office as that amount included use of office equipment, secretary/receptionist, and telephone system. The Commission agrees with Staff's assessment of the office situation and concludes that Staff's adjustment is fair and reasonable. The Commission therefore adopts Staff's adjustment.

(c) Brookside included in its Application an expense adjustment of $46,090 for salary for Mr. Nutt. Staff witness Maready testified that the Staff denied the salary expense due to the Commission's Order in the last rate case where the Commission granted an operating margin that sufficiently included profits in lieu of a salary. Company witness Nutt testified that he is responsible for the day-to-day management of the Company's wastewater treatment operations including the provision of necessary engineering services and supervision of environmental compliance. Mr. Nutt also stated that he serves as business manager of the Company and handles customer, vendor, and contractor relations. Mr. Nutt offered that Brookside is in the process of becoming incorporated and a reasonable salary expense would be less confusing and more realistic to the Company's profit and loss statement than allowing a higher operating margin in lieu of a salary.

In consideration of this item, the Commission is of the opinion that a reasonable management salary should be added as a cost of service item. Brookside included a management salary of $46,090 in its Application. Mr. Nutt testified regarding his duties in the management of Brookside and gave examples of the work that he performs. Upon weighing the testimony, the Commission concludes that Brookside's adjustment to include a management fee in the amount of $46,090 should be accepted. Therefore, the Commission approves the salary expense of $46,090. Implicit with the approval of the salary expense is the related expense item for Social Security Taxes in the amount of $3,526.

(d) Brookside included in its Application an adjustment of $2,000 for rate case expenses. Brookside also explained that this amount was estimated at the time of filing and further that Brookside had amortized the expenses over three (3) years. At the hearing, Brookside presented Hearing Exhibit No. 1 which was an affidavit setting forth the amount of attorney's fees incurred during this rate case. Hearing Exhibit No. 1 indicates that Brookside's rate case expenses have amounted to $9,000 in this case. Staff had accepted the $2,000 adjustment as reasonable.

The Commission believes the updated and verifiable rate case expenses are reasonable and approves amortization of the rate case expense over three (3) years. The Commission therefore adopts the Company's adjustment of $3,000 for rate case expense.

Based on the stipulation of the Company, the Commission hereby approves all other Staff adjustments. Utilizing the adjustments approved herein, the Commission concludes that the Company's appropriate operating expenses for the test year, after accounting and pro forma adjustments, are $86,985.

5. Based on the accounting and pro forma adjustments herein approved, the Commission concludes that Brookside's appropriate total income (loss) for return for the test year is calculated to be ($18,945). The calculation of total income for return is shown in Table A.

TABLE A
TOTAL INCOME FOR RETURN

Operating Revenues	$ 68,040
Operating Expenses	86,945
Net Operating Income (Loss)	$ (18,945)
Customer Growth	-0-
Total Income for Return (Loss)	$ (18,945)

6. Under the guidelines established in the decisions of Bluefield Water Works and Improvement Co. v. Public Service Commission of West Virginia, 262 U.S. 679 (1923), and Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591 (1944), this Commission does not ensure through regulation that a utility will produce net profits. As the United States Supreme Court

noted in Hope, a utility "has no constitutional rights to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures." However, employing fair and enlightened judgment and giving consideration to all relevant facts, the Commission should establish rates which will produce revenues "sufficient to assure confidence in the financial soundness of the utility and ... that are adequate under efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties." Bluefield, supra, at 692-693.

There is no statutory authority that prescribes the method which this Commission must utilize to determine the lawfulness of the rates of a public utility. For a sewer utility whose rate base has been substantially reduced by customer donations, tap fees, contributions in aid of construction, and book value in excess of investment, the Commission may decide to use the "operating ratio" and/or "operating margin" method for determining just and reasonable rates. The operating ratio is the percentage obtained by dividing total operating expenses by operating revenues; the operating margin is determined by dividing the net operating income for return by the total operating revenues of the utility. This method was recognized as an acceptable guide for ratemaking purposes in Patton v. South Carolina Public Service Commission, 280 S.C. 288, 312 S.E.2d 257 (1984). The Commission will use the operating margin as its guide for determining the lawfulness of Brookside's rates. The Commission believes that the operating margin will provide an acceptable and fair guide for determining rates in this proceeding.

7. Based on the Company's gross revenues for the test year, after accounting and pro forma adjustments approved herein, under the presently approved schedules, the Company's operating expenses for the test year, after accounting and pro forma adjustments approved herein, and customer growth, the Company's present operating margin is shown in Table B as follows:

TABLE B
OPERATING MARGIN

BEFORE RATE INCREASE:

Operating Revenues	$ 68,040
Operating Expenses	86,985
Net Operating Income	$ (18,945)
Customer Growth	-0-
Total Income for Return	$ (18,945)
Operating Margin	(27.84%)

8. Applying the adjustments approved in this Order to the Company's proposed schedule of rates, the Commission calculates that Brookside's proposed increase would result in an operating margin of 21.16%. Table C illustrates an operating margin of 21.16% and shows the effect of the Company's proposed increase, after the accounting and pro forma adjustments approved herein.

TABLE C
OPERATING MARGIN

AFTER PROPOSED (FULL) RATE INCREASE:

Operating Revenues	$ 119,095
Operating Expenses	93,893
Net Operating Income	$ 25,202
Customer Growth	-0-
Total Income for Return	$ 25,202
Operating Margin	21.16%

The Commission is mindful of the standards delineated in the Bluefield decision and of the need to balance the respective interests of the Company and of the consumers. It is incumbent upon this Commission to consider not only the revenue requirement of the Company but also the proposed price for the sewer service, the quality of the sewer service, and the effect of the proposed rates upon the consumer. See, Seabrook Island Property Owners Association v. South Carolina Public Service Commission, 303 S.C. 493, 401 S.E.2d 672 (1991).

The three fundamental criteria of a sound rate structure have been characterized as follows:

> ... (a) the revenue-requirement of financial-need objective, which takes the form of a fair-return standard with respect to private utility companies; (b) the fair-cost apportionment objective which invokes the principle that the burden of meeting total revenue requirements must be distributed fairly among the beneficiaries of the service; and (c) the optimum-use or consumer rationing under which the rates are designed to discourage the wasteful use of public utility services while promoting all use that is economically justified in view of the relationships

between costs incurred and benefits received.

Bonbright, Principles of Public Utility Rates (1961), p. 292.

In its determination that the proposed schedule of rates presented by the Company is excessive and unreasonable, the Commission has considered the proposed increase in light of the various standards to be observed and the various interests represented before the Commission. The Commission is mindful that it must balance the interests of the Company -- i.e. the opportunity to make a profit or earn a return on its investment, while providing adequate sewerage service -- with the competing interests of the ratepayers -- i.e. to receive adequate service at a fair and reasonable rate. The Commission, in balancing these competing interests, believes that an operating margin of 21.16% is unreasonable and excessive and, therefore, has determined that the proposed schedule of rates is unjust and unreasonable and thus inappropriate for the Company and the ratepayers.

It is therefore incumbent upon the Commission to address and determine a reasonable operating margin for the Company. Based on the considerations enunciated in Bluefield and Seabrook Island, on the fundamental criteria of a sound rate structure as stated in Principles of Public Utility Rates, and on the competing interests of the Company and the ratepayers, the Commission determines that the Company should have the opportunity to earn an operating margin of 12.29%. In order to have a reasonable opportunity to earn an operating margin of 12.29%, the Company will need to produce $103,320, or an additional $35,280 in annual operating revenues. Therefore, the Commission approves additional revenues of $35,280. Table D illustrates a 12.29% operating margin.

TABLE D
OPERATING MARGIN

AFTER APPROVED RATE INCREASE:

Operating Revenues	$ 103,320
Operating Expenses	90,621
Net Operating Income	$ 12,699
Customer Growth	-0-
Total Income for Return	$ 12,699
Operating Margin	12.29%

9. In fashioning rates to give the Company the required amount of operating revenues so that it will have the opportunity to earn a 12.29% operating margin, the Commission has carefully considered the needs of the Company's customers with the needs of the Company. The Commission is aware that the customers do not want to pay higher rates, but the Commission is also cognizant that the Company must have the necessary revenues with which to operate and to provide quality service. The Commission encourages the Company to continue to provide quality service to its customers. The rates designed herein consider the quality of service provided by the Company to its customers, the need for the continuance of the provision of adequate service, and the need of the Company to meet its financial obligations, as well as the impact of the increase on those customers receiving the service.

The Commission concludes that an increase in rates is necessary. Accordingly, the Commission will design rates which will increase the flat monthly rate from $13.50 to $20.50 for residential customers. The Commission also establishes a commercial rate of $20.50 per SFE (Single Family Equivalent). These rates will afford Brookside the opportunity to earn a 12.29% operating margin.

Further, it appears that the Company has justified its request for establishment of a Tap Fee and an increase in the New Customer Account Charge. The Commission concludes that Brookside may implement a Tap Fee of $400 per SFE for new connections outside of the Brookside Village subdivision and may increase the Customer Account Charge to $20.00.

Based upon the above considerations and reasoning, the Commission hereby approves the rates and charges as stated above and as attached hereto as Appendix A. The Commission finds and concludes that the rates and charges approved herein are just and reasonable. These rates and charges are designed in such a manner so as to produce and distribute the necessary revenues to provide the Company the opportunity to earn the approved operating margin of 12.29%.

IT IS THEREFORE ORDERED THAT:

1. The rates and charges attached on Appendix A are approved for service rendered on or after the date of this Order. The rate schedule is hereby deemed to be filed with the Commission pursuant to S.C. Code Ann. §58-5-240 (Supp.1995).

2. The Company is granted the opportunity to earn an

operating margin of 12.29%.

3. Should the approved schedule not be placed in effect before the expiration of three (3) months after the effective date of this Order, then the approved schedule may not be charged without written permission of the Commission.

4. The Companies shall maintain their books and records for sewer operations in accordance with the NARUC Uniform System of Accounts for Class B Sewerage Utilities, as adopted by this Commission.

5. It is further ordered that the Company should add its telephone number to the bill form that is sent to the customer each month.

6. Further, the Company is encouraged to improve communication with the customers.

7. This Order shall remain in full force and effect until further Order of the Commission.

BY ORDER OF THE COMMISSION:

Rudolph Mitchell
Chairman

ATTEST:

Charles W Ballentine
Executive Director

(SEAL)

APPENDIX A

BROOKSIDE SEWER DISTRICT
4 WINDMILL DRIVE
WELLFORD, SC 29385
(803) 439-0820

FILED PURSUANT TO:

DOCKET NO. 95-1171-S

ORDER NO. 96-134

DATED: FEBRUARY 29, 1996

RATES EFFECTIVE: FEBRUARY 29, 1996

SEWER SERVICE

RESIDENTIAL - monthly charge per single-family house, condominium or mobile home:	$20.50
COMMERCIAL - monthly charge	$20.50 per SFE
TAP FEE (new connections only outside Brookside Village subdivision)	$400.00 per SFE
NEW CUSTOMER ACCOUNT CHARGE This is a one-time fee charged to each new account to defray the cost of initiating service.	$20.00